

STATE OF MAINE
PUBLIC UTILITIES COMMISSION

Docket No. 98-161

December 11, 1998

OLDE PORT MARINER FLEET, INC.
Complaint Regarding Casco Bay
Island Transit District's Tour
and Charter Service

FINAL ORDER

WELCH, Chairman; NUGENT and DIAMOND, Commissioners

I. INTRODUCTION

In this Order, the Commission: (1) finds that Casco Bay Island Transit District (CBITD) has properly sized its fleet for regular route service; (2) institutes new record keeping requirements for CBITD; (3) institutes a new process for notifying the Commission of CBITD's intention to acquire a new vessel; (4) finds that CBITD and Olde Port Mariner Fleet, Inc. (OPMF) compete in the same market for charters of fewer than 150 passengers; (5) finds that CBITD does not have an undue advantage because of its ability to price its small charters at marginal costs;¹ (6) defines the term "incidental tour and charter"; and (7) commits to institute a rulemaking to revise Chapter 520 of our Rules.

II. PROCEDURAL HISTORY

On February 24, 1998, the Commission received a complaint from OPMF alleging that CBITD was using funds from its regulated business to purchase a vessel for use in unregulated tour and charter activities. On February 27, 1998, CBITD filed a Petition Under 35-A M.R.S.A. §§ 902, 1101 For Approval of a Loan and Pledge of Assets with the Commission relating to the purchase of a new vessel, the *Bay Mist*. The Petition was given a separate docket, Docket No. 98-147. On March 3, 1998, the Commission sent a letter to CBITD requesting a response to the complaint within 10 days pursuant to 35-A M.R.S.A. § 713. In particular, the Commission requested that CBITD explain how Mr. Libby's complaint related to the purchase of the *Bay Mist*. On March 11, 1998, CBITD filed its response to OPMF's complaint. On March 19, 1998, both CBITD and OPMF filed supplemental letters further detailing their positions. On March 23, 1998, CBITD filed an additional response to OPMF's March 19th filing.

¹Commissioner Diamond dissents from this finding. See attached Dissenting Opinion.

On March 23, 1998, the Commission approved CBITD's Petition for Approval of a Loan and Pledge of Assets. During its deliberations, the Commission determined that the complaint filed by OPMF raised issues which warranted further investigation. Thus, on March 26, 1998, the Examiner issued a procedural order delineating the scope of this Investigation. Specifically, the procedural order stated that the Commission had opened this Investigation pursuant to 35-A M.R.S.A. § 713 which precludes a utility from charging its rate payers for costs attributable to unregulated business ventures undertaken by the utility. 35-A M.R.S.A. § 713. The procedural order also noted that Section 713 also requires the Commission to attempt to ensure that no utility has an undue competitive advantage in a competitive market due to its utility status. Finally, the procedural order granted the petitions to intervene of Bay View Cruises and Personal Touch Catering. The OPA intervened as a matter of right on March 27, 1998.

On October 2, 1998, and October 8, 1998, hearings were held in this matter. OPMF, OPA, and CBITD each filed opening briefs on October 27, 1998, and reply briefs on November 3, 1998.

III. APPLICABLE STATUTORY PROVISIONS

A. CBITD's Enabling Legislation

Prior to 1981, CBITD's predecessor, Casco Bay Lines, provided both ferry service and tour and charter service to the islands of Casco Bay, although it overemphasized the tour and charter business to the detriment of regular route customers. When Casco Bay Lines declared bankruptcy in 1980, the islanders worked to create a transportation district which would be run by the islanders and which would focus on the provision of regular route service to the islands of Casco Bay. As a result, the Legislature created CBITD by a special act in 1981. CBITD is a rate payer-owned public utility with authority to:

do things necessary to furnish waterborne transportation in this area, including incidental tour and charter service, for public purposes in the interest of public health, safety, comfort and convenience of the inhabitants of the islands comprising the district.

Private and Special Laws 1981 Ch. 22, § 1.

One of the central disputes in this Investigation is what the Legislature intended when it included the phrase "incidental tour and charter" in the enabling legislation. OPMF and OPA believe the phrase is "a restriction that was included to

ensure that CBITD did not repeat the sins of its predecessor CBL by emphasizing tour and charter services over its responsibility to provide regularly scheduled ferry service . . ." CBITD argues that inclusion of the phrase was a recognition that tour and charter revenues provided "significant support" to regular route operations and that it was important that CBITD be permitted to continue that business. This issue will be discussed and resolved in its entirety below.

B. 35-A M.R.S.A. § 713 and Chapter 820

In May 1997, the Legislature enacted L.D. 502, "An Act to Require Fair Compensation for Rate Payer Assets Used by a Subsidiary or Affiliate of a Utility." This Act is codified in sections 707, 713, 714 and 715 of Title 35-A. The Legislature was concerned about electric and gas companies' diversification into unregulated activities. See L.D. 502, Summary (118th Legislature 1997). Given the relatively risky nature of entering competitive markets, the Legislature wanted to ensure that the costs of any such ventures were not borne by the utility's rate payers.

At issue in this case is the application of Section 713 to CBITD and its incidental tour and charter business. Section 713 provides:

A utility may not charge its rate payers for costs attributable to unregulated business ventures undertaken by the utility or an affiliated interest. The Commission shall allocate between a utility's shareholders and ratepayers, costs for facilities, services or intangibles, including good will or use of a brand name, that are shared between regulated and unregulated business activities. The Commission shall also attempt to ensure that the utility or the affiliated interest does not have an undue advantage in any competitive market as a result of its regulated status or its affiliation with a regulated utility.

35-A M.R.S.A. § 713. Thus, Section 713 precludes a utility from charging its rate payers for costs attributable to unregulated business ventures undertaken by the utility and requires that the Commission attempt to ensure that no utility has an undue competitive advantage in a competitive market due to its utility status. Id.

Chapter 820 of our Rules, Requirements for Non-Core Utility Activities and Transactions between Affiliates,

incorporates the principles established in *Robert D. Cochrane v. Bangor Hydro-Electric Company, Request for Commission Investigation into Bangor Hydro-Electric Company's Practice of Installing or Monitoring Security Alarm Systems*, Docket No. 96-053 (Jan. 28, 1997) and effectuates the requirements of L.D. 502. While the statutory provisions associated with L.D. 502 apply to all utilities generally, consumer-owned utilities, as defined in 35-A M.R.S.A. §§ 3501 and 6101, are exempt from Chapter 820. While CBITD does not specifically meet either definition of a consumer-owned utility because it is neither an electric company nor a water utility, CBITD is a consumer-owned water transportation utility -- the only one in the state.

In promulgating Chapter 820, we did not contemplate the application of Chapter 820 to CBITD and if we had, we likely would have specifically exempted it because CBITD does not have an incentive to shift costs for the benefit of its shareholders and to the detriment of its rate payers because its shareholders and rate payers are identical. Thus, we decline to apply the specific standards set forth in Chapter 820 to CBITD.

C. Conflicting Nature of the Applicable Statutes

The Commission must find a way to effectuate the policy goals of the applicable statutes -- despite the fact that those goals often conflict with one another. We recognize that CBITD's enabling legislation made clear that the Legislature authorized CBITD's participation in non-regulated activities. On the other hand, the Legislature has also stated that the Commission must ensure that public utilities do not use their regulated status as a means to compete unfairly in competitive markets. Our decision today reflects our best effort at effectuating the Legislature's intended policies. The parties should recognize that if they disagree with our decision, the Legislature may be the proper place for resolution of these conflicts in the underlying goals and policies of the legislation.

IV. CBITD MUST PROPERLY SIZE ITS FLEET FOR REGULAR ROUTE SERVICE

As stated earlier, this Investigation resulted from a complaint by OPMF that CBITD had improperly acquired a new vessel, the *Bay Mist*, for use in providing tour and charter service. As this Investigation has unfolded, the sizing of CBITD's fleet for regular route service has emerged as one of the most important issues in this case. Indeed, whether CBITD's tour and charter services are incidental to its regular route service turns on the determination of whether CBITD's fleet is correctly sized. For the reasons set forth below, we find that CBITD currently requires four vessels plus a spare to provide regular route service.

A. CBITD's Methodology For Sizing Its Fleet

CBITD provides year-round passenger ferry service to six islands in Casco Bay. CBITD claims that it needs five interchangeable vessels to provide safe, reliable, economical, year-round, regular route service -- four vessels for regular route service and one vessel as a spare.

Prior to the acquisition of the *Bay Mist*, CBITD's fifth vessel was the *Quickwater*, a specialized, small vessel which was purchased in 1995 pursuant to an agreement with McKinley Partners Limited Partnership (MPLP) to increase service to Diamond Cove on Great Diamond Island. As will be discussed in more detail below, ridership from Diamond Cove grew much more quickly than expected and by 1996 the *Quickwater* was unable to provide the necessary service. CBITD used one of its other regular route vessels to provide service to Diamond Cove and the *Quickwater* became CBITD's spare vessel. However, the *Quickwater's* limited capacity and single deck made it largely unsuitable for regular route service, even as a spare. Thus, in 1997, CBITD determined that it needed to sell the *Quickwater* and acquire another vessel that would be more suitable to CBITD's needs and be interchangeable with its other vessels. Based on its perceived need for a fifth, interchangeable vessel and the inadequacies of the *Quickwater*, CBITD both purchased the *Bay Mist* and sold the *Quickwater* in 1998.

CBITD claims that its decision to purchase the *Bay Mist* was made solely to satisfy its needs to supply regular route service (not for use in its unregulated tour and charter business). CBITD points to four factors it uses to determine the appropriate size for its fleet.

1. Vessel Size

CBITD claims that it sizes its vessels to meet the requirements of its year-round regular route service in a safe, reliable and economic manner. Based on its year-round experience, the District claims that its vessels should: (1) be 65-85 feet in length; (2) have a 200-300 passenger capacity to handle its current regular summer capacity; (3) be constructed of steel to operate in different seasonal conditions (including cold, windy and stormy weather in the winter); and (4) have two passenger decks. A two-deck vessel is important because the tides in Casco Bay vary significantly (10 feet to 14 feet). This condition, coupled with a fixed pier requirement at the islands, necessitates two-deck vessels to handle the distance between water height and the pier deck depending on the tide, to keep the ramp angle controlled within safe limits.

2. Interchangability

CBITD states that its vessels must be interchangeable, i.e. each vessel must be able to serve all of CBITD's stops, in order to ensure a seamless transfer to another vessel if one vessel breaks down. It is important that CBITD be able to maintain its schedule. A spare vessel which could only service some of its stops would hamper CBITD's efforts to provide reasonable, reliable service to its rate payers.

3. The need for a spare vessel

CBITD claims that it needs a spare vessel to ensure reliable service in the event one of the vessels in regular route service breaks down or there is a demand for additional capacity of scheduled runs. All parties agreed with this claim.

4. The need to meet peak capacity and multi-stop schedule

CBITD believes that to fulfill its mission of providing transportation in Casco Bay, it must maintain the vessel capacity necessary to accommodate the peak passenger loads. CBITD notes that these peak loads occur during relatively short periods of the year, week, and day.

CBITD also claims that it must accommodate a complex, multi-stop ferry schedule which is dictated by the needs of the islanders, its regular route service passengers. CBITD must develop a schedule which takes into consideration the number of stops, the distance between stops, the frequency of service, the demand for service, the relative demand of the different stops, the weather, and the amount of freight. Some of these factors are more significant than others; some are consistent with one another, others are not. Thus, a positive change in one factor often results in a negative change in another. CBITD argues that establishing a complex schedule which provides the maximum benefit to the most people at the minimum acceptable cost requires a subjective balancing of the various factors.

CBITD also notes that its current regular route service schedule was developed over a long period of time with a great deal of input from the islanders, both directly and indirectly through their elected representatives on the Board of Directors.² CBITD claims that the schedule has become a standard of service upon which the islanders rely and around which they

²CBITD's Board of Directors includes representatives from each of the islands that CBITD serves.

plan their lives. CBITD believes that the islanders have demonstrated a strong consensus that they want and will pay for the current level of service, which includes not only the schedule but also the size and configuration of the various vessels.

B. OPMF's Criticism of CBITD's Fleet Size

OPMF argues that CBITD intentionally oversized its fleet through the purchase of the *Bay Mist*. OPMF contends that CBITD does not need five vessels to provide adequate regular route service and that CBITD will use its excess capacity to compete unfairly in the tour and charter market. OPMF has requested that the Commission order CBITD to sell the *Bay Mist*.

OPMF witness Mr. Bruzzone claims that two vessels, rather than the three currently used by CBITD, can adequately and effectively serve the Down Bay market.³ To support his claim, Mr. Bruzzone analyzed CBITD's demand during the 7:00 - 9:30 a.m. and 4:00 - 6:00 p.m. peak periods. Based on his analysis, Mr. Bruzzone testified that CBITD has a capacity of 998 passengers, but only carries 140 passengers during the peak afternoon period -- a load factor of 14%, which is actually lower than the average 26% load factor during the rest of the day. Mr. Bruzzone further testified that:

Throughout the day the normal course of service is two boats on the down bay service. In peak period they add an extra trip. They add an extra boat into service. What I'm telling you is that I don't think that the demand warrants an extra boat in service.

Thus, Mr. Bruzzone claims that CBITD's current fleet effectively gives it two spare vessels. Mr. Bruzzone proposes a two boat schedule which combines Diamond Cove and Long Island into one trip because they make up about half of the Down Bay patronage. Mr. Bruzzone reasons that because these stops are relatively close together, in the morning the boat can stop at Diamond Cove, drop-off and pick-up, go directly to Long Island and then return directly to Portland. In the afternoon, the same pattern would be used. According to Mr. Bruzzone, the only significant change between this schedule and CBITD's would be the reduction of one morning trip from Great Diamond; the existing midday service would be unchanged.

OPMF witness Mr. Ashton also examined CBITD's ridership and supports Mr. Bruzzone's claim that only two vessels are

³Down Bay service includes Great Diamond, Little Diamond, Chebeague, Cliff and Long Islands.

needed to serve the Down Bay run. Mr. Ashton examined the rate of growth in ridership and testified that it had increased less than .71% in the last three years. On that basis, he concluded that CBITD did not need to purchase the *Bay Mist* to meet anticipated growth. Mr. Ashton claims that CBITD has increased its capacity more than 40% in the last six years while its ridership demand increased only 13% during that same period.

Finally, Mr. Ashton claims that the *Bay Mist* exacerbated an already significant problem of excess capacity. Mr. Ashton analyzed CBITD's peak demand on days during the period from 1995-1997 in which service on regulated routes was at or near capacity and found that CBITD vessels were at full capacity less than 3% of the time. Mr. Ashton also reviewed several days during the peak summer period and claims that the fleet was rarely fully utilized even on the busiest days. Ridership data from July and August 1995-1997 indicate that average ridership was less than 25% of CBITD's capacity.

C. OPA's Position

The OPA claims that the record indicates that CBITD did not purchase the *Bay Mist* for its regular route needs but instead to regain the tour and charter business it lost when the *Quickwater* was used as CBITD's spare vessel. Further, OPA believes CBITD's decision to replace the *Quickwater* with a larger vessel was not based on regular route needs but on its obligations to MPLP. The OPA claims that testimony by Mr. Christian indicates that the tour and charter aspects of CBITD's service were a "major factor" in the decision to buy the *Bay Mist*.

D. The Role of CBITD's Contract With MPLP In The Size of CBITD's Current Fleet

In 1995, CBITD signed a contract (Agreement) with McKinley Partners Limited Partnership (MPLP) concerning the provision of ferry service to MPLP's real estate development on Great Diamond Island, Diamond Cove. Prior to the contract, service to Diamond Cove was limited to two stops a day. MPLP, however, wanted more regularly scheduled ferry service to Diamond Cove so that it could market its project as being regularly served by CBITD.

Because the demand for service was not sufficient to warrant the level of service desired by MPLP, CBITD agreed to add several more stops as part of its regular route schedule and to offer supplemental service (consisting initially of six new trips per day in the summer) if MPLP would agree to:

- (1) subsidize the service through agreed upon yearly payments for the projected operating losses CBITD would incur in providing the new service;
- (2) provide the cash necessary to purchase a small high speed vessel (the *Quickwater*) which would be used to provide almost all of the service to Diamond Cove;
- (3) reimburse CBITD for the costs associated with purchasing floats for the *Quickwater* to use both in Portland and at Diamond Cove;
- (4) maximize its use of CBITD services by utilizing available scheduled passenger, freight, and vehicle transport services; and
- (5) use CBITD's charter services and encourage all travelers to Diamond Cove and all commercial establishments transporting passengers, freight or vehicles to Diamond Cove to use the services of CBITD to the maximum extent possible.

The parties also agreed to terminate the Agreement in 2000.

Since 1995, CBITD has provided service to Diamond Cove as required by the Agreement and MPLP has fulfilled its obligations. The Agreement has been modified numerous times; some of the scheduled runs which were initially supported by MPLP have become self-supporting due to a great increase in ridership since 1995. In addition, during the summer of 1998, CBITD and MPLP agreed to drop the requirement that MPLP use CBITD's charter services and encourage others to do the same. Further, as described earlier, because ridership grew much more dramatically than originally anticipated, the *Quickwater* was unable to service all of the Diamond Cove traffic, which ultimately led to the purchase of the *Bay Mist* in 1998.

Notwithstanding the possibility that the Agreement led CBITD to expand more rapidly than would otherwise have been the case, the operative issue before us remains whether the fleet is properly sized at the present time. Given our conclusion on that issue, we see no need for an extended discussion of the merits of the Agreement. We would, however, offer two brief observations.

First, we are troubled by the provision in the Agreement linking regular ferry service with unregulated charter service, something contrary to the principles of fair competition and the underlying policies of Section 713. As OPA witness Mr. Rubin testified, CBITD should not be allowed to leverage its

position as the only regular ferry provider to obtain an advantage in the competitive tour and charter market. Indeed, CBITD witness Mr. Silkman, OPA witness Mr. Rubin, and OPMF witness Mr. Ashton all agreed that CBITD's tie-in arrangement with MPLP was inappropriate.

As noted above, in the summer of 1998, as a result of the concerns raised in this proceeding, CBITD determined that the tying provision was no longer necessary.⁴ Accordingly, the contract was amended and the tying provision was removed. If that provision had not been removed, we likely would have declared that portion of the contract null and void as an undue advantage pursuant to section 713.

Second, the practice of allowing private parties to subsidize ferry routes should be approached with great care. We recognize that a developer of island properties may confront a classic chicken and egg problem, in that people may not wish to purchase property absent frequent ferry service and the ferry may not wish to provide such service absent a sufficient customer base. While it is understandable that the developer may be willing to subsidize the ferry service under these circumstances, problems can arise if the development proves less successful than anticipated and the developer is unable to continue providing financial support. This may leave the ferry with customers who purchased property and even relocated families based on the expectation of a level of service that cannot be justified without the private subsidy. More relevant to the instant case, it may also lead the ferry to have more excess capacity than would have occurred without the subsidy.

As noted above, we need not deal with the reasonableness of private subsidies in light of our conclusion with respect to the sizing of the fleet. Our inaction should not, however, be construed as an endorsement or condemnation of the practice.

E. Decision on Fleet Sizing

1. CBITD's current fleet is properly sized.

⁴ CBITD contends it has never conceded that the provision was improper or had an anti-competitive effect. Rather, CBITD believed that the provision had always been insignificant, became irrelevant, and that there was no need to continue the provision if someone was concerned about it. Thus, the termination of the provision was made orally in early July and confirmed in a written amendment in September.

We find that that CBITD's five vessel fleet is properly sized to provide its regular route service. While we agree with OPMF that the five vessel schedule contains considerable excess capacity, we also agree with CBITD that such extra capacity is a necessary consequence of its obligation to provide year-round reliable service. Accordingly, we will not order CBITD to sell the *Bay Mist*.

OPMF has not proven that there is excess capacity over and above that required to serve regular route service in Casco Bay. Mr. Bruzzone admitted on cross examination that his analysis of the average load factor was not based on peak service demands data. He also admitted on cross examination that when sizing a fleet, it must be sized to meet the maximum, not the average, demands of each season. Mr. Ashton's testimony on this subject deals with growth in ridership and demand but does not consider that the Casco Bay system is a complex ferry system that requires the consideration of many different factors in determining the proper schedule and size of its vessels. Neither Mr. Ashton nor Mr. Bruzzone addressed the complexities of CBITD's schedule, although Mr. Bruzzone did agree with all the factors considered by CBITD in sizing its system.

Absent a clear showing of excess capacity by the OPMF, we find that CBITD has correctly sized its fleet for regular route service. CBITD has adequately supported its assertions that it has sized its system to meet the level of regular route service required by its customers and that five interchangeable vessels are necessary to meet its scheduling needs and peak load demand.⁵ Therefore, we conclude that CBITD's five vessel fleet is properly sized and that it need not sell the *Bay Mist*.

2. New record-keeping procedures will ensure that future fleet additions are appropriate.

One of the major problems in assessing whether CBITD has properly sized its fleet to meet the requirements of its regular route passengers is that CBITD's records do not adequately distinguish regular route customers from tour and charter passengers. CBITD witness Mr. Mavadones testified that the only way CBITD has to distinguish regular rate customers and tourists is by the questions they ask at the ticket booth.

⁵We reject OPMF's argument that CBITD should enter a long-term contract with another carrier to provide regular service during peak periods. We are persuaded by CBITD's argument that such a solution is not feasible over the long term because of passenger dislike for the smaller vessels, the inability of the vessels to dock at CBITD's piers, and problems with CBITD's union and insurer.

Mr. Mavadones also testified that CBITD has no systematic process to predict peak periods of use of its fleet and relies on the intuition of its operators to stop selling tour tickets if they anticipate that a particular run may reach capacity. CBITD witness Mr. Christian confirmed CBITD's lack of systematic analysis of its peaks by testifying that, "everyone knows we have to take care of the regular ridership first. . . and once we have a feel for that then we try to sell the rest of the capacity and try not to push it to its limits."

The problem with CBITD's inability to distinguish tour customers from regular riders is exacerbated by the fact that CBITD intentionally inserts its charter passengers into its regularly scheduled service during peak periods. The record indicates that:

- (1) CBITD frequently schedules charter passengers to return to Portland on its regularly scheduled service during peak periods;
- (2) Charters are scheduled during periods of peak simultaneous use;
- (3) Lobster Bake groups are scheduled to Peaks Island on Friday and Saturday during peak hours;
- (4) Charters transported in a group to a destination island are scheduled to return at staggered times on regularly scheduled trips, including during peak hours; and
- (5) Groups of twenty or more are sold transportation at group rates on regularly scheduled trips, including trips during peak hours.

Mr. Christian also testified that once tour and charter passengers get out on the islands, CBITD cannot control when they come back. Because of this lack of control, tour and charter passengers are able to return to Portland during peak times.

As discussed above, CBITD claims that it must size its fleet to meet peak capacity needs of its regular route customers. If CBITD cannot distinguish its regular route customers from tour and charter travelers, it cannot realistically make determinations regarding the scheduling needs of its regular route customers. While it is entirely reasonable to add a run because a considerable number of island residents

need to get to work by a certain time, it is not reasonable to try to justify the addition of another run based upon islander needs when 80% of the passengers on the boats are tourists who could adjust their plans to meet CBITD's schedule or are lobster bake or charter passengers who could have their needs met through charter services.

During the hearing, OPA witness Scott Rubin testified to the danger of allowing CBITD to "dump" tour and charter passengers into peak time regular route runs. Such a practice allows CBITD to artificially inflate its regular route needs and potentially acquire unneeded regular route capacity which actually gets used for tour and charter business. Given the evidence described above, we see the continued potential for CBITD to overestimate its regular route needs based upon tour and charter use of the system during peak times.

Today we adopt a new standard for CBITD to meet with its record keeping. We do not prohibit CBITD from continuing the practices described earlier; to some extent they are proper and economically sound ways to utilize CBITD's spare capacity. We must ensure, however, that CBITD does not use this practice to improperly expand its fleet. Thus, we will institute new record keeping requirements as well as a new procedure for Commission approval of the acquisition of a new vessel.

a. New record keeping requirements

First, with regard to record keeping, CBITD must be able to distinguish the number of tickets sold to its "regular route customers" and all other passengers, including tour and charter passengers. We will leave it to CBITD to decide upon the specific definition of "regular route customers" although at a minimum CBITD should include in that definition island residents (both summer and year-round), property owners, and employees of island businesses.

Once it defines its regular route customer, CBITD must design a record-keeping system which will allow it to distinguish, for every run on each vessel, the number of regular route customers from all other passengers. It may be necessary for CBITD to sell tour and charter tickets from a separate window as suggested by the OPA or perhaps to issue some sort of special identification to "regular route customers." We leave the details to CBITD and require it to file both its definition and its proposed record-keeping system no later the **March 15, 1999**.

b. CBITD must file any request for financing to purchase a new vessel with sufficient time for Commission review.

CBITD must file any request for approval of financing a new vessel purchase pursuant to 35-A M.R.S.A. §§ 901-902, at least 60 days before the intended closing date. The Commission may take additional time beyond 60 days to determine the matter if it concludes additional time is necessary pursuant to 35-A M.R.S.A. § 902(3). In addition to providing details regarding the vessel and the financing associated with the vessel, CBITD must demonstrate that the peak regular route needs of its ratepayers require the acquisition of a new vessel. The Commission will review CBITD's request to ensure that tour and charter passengers have not been used to justify the need for additional regular route capacity.

VI. APPLICATION OF SECTION 713 TO CBITD'S TOUR AND CHARTER BUSINESS

As indicated in Section III above, the parties disagree regarding how Section 713 should be applied to CBITD. The resolution of the parties' disagreement will require the resolution of one of the fundamental underlying issues in this case: whether CBITD should base its tour and charter service prices on fully allocated costs. It will also require a determination of the intent of Section 713, whether CBITD and OPMF compete in the same market, and whether CBITD has any undue advantage in the tour and charter market.

A. General Intent of Section 713

In the early 1990s, regulated utilities, especially electric and gas utilities, began to expand their businesses to provide unregulated services in competitive markets. See L.D. 502, Summary (118th Legislature 1997). The Legislature enacted Section 713 to protect utility rate payers from the risks associated with a utility's involvement in unregulated activities. The Legislature recognized that an investor-owned utility's shareholders might have an incentive to shift losses associated with unregulated ventures to rate payers by raising rates for regulated services to cover any losses incurred in unregulated activities. The Legislature also recognized that a utility could use its status as a regulated utility, which carries both non-financial and financial benefits, to gain an unfair advantage in a competitive market.

Thus, the Legislature instituted three types of protections through Section 713. The Legislature protected rate payers by: (1) prohibiting the utility from charging its rate payers for costs attributable to the unregulated ventures; (2) requiring the Commission to allocate costs between the utility's rate payers and its shareholders; and (3) mandating that the

Commission attempt to ensure that utilities do not have an "undue advantage" in the competitive market.

The parties disagree regarding: (1) how the term "attributable" should be interpreted (does it require a marginal cost study or a fully allocated cost study?) (2) whether the fully allocated cost requirement of the second protection applies to CBITD because it does not have shareholders; and (3) how the term "undue" should be defined and what remedy should be applied if it is determined that CBITD has an undue burden.

B. Section 713 Does Not Require CBITD to Use Fully Allocated Cost Accounting

The first issue which must be resolved is how CBITD should account for the costs associated with providing tour and charter service. Issues relating to the pricing of tour and charter service will be addressed in Section C below.

1. CBITD's Position

CBITD claims that by using the term "attributable," the Legislature intended only a marginal cost standard which CBITD already satisfies with its Island Revenue Expense Analysis (IREA) and by setting its tour and charter rates at more than twice marginal cost. CBITD argues that the Legislature would have used the word "allocable" or specifically referred to shared costs or other similar words if it intended the first sentence to require an allocation of fixed/shared costs instead of a marginal cost standard.

CBITD then argues that the fully allocated cost requirement of the second protection applies only to investor-owned, for-profit utilities and not to non-investor owned, not-for-profit quasi-municipal utilities such as itself. CBITD points out that quasi-municipal utilities have no shareholders and therefore all profits from non-regulated activities flow directly to the ratepayers. Further, quasi-municipal, not-for-profit utilities face a tougher standard than fully allocated costs; they cannot provide any service, regulated or non regulated, without express legislative authorization. Thus, according to CBITD, because quasi-municipal, not-for-profit utilities can provide only services that the Legislature has found to be necessary and in the public interest, the fully allocated cost standard need not apply.

2. OPMF's Position

OPMF believes that CBITD's method of interpreting Section 713 by separating each of the sentences and interpreting them in isolation violates the basic tenet of legislative interpretation which requires that each part of a statute be read together to the extent possible to reach a result which is internally consistent. See State v. Rand 430 A.2d 808 (Me. 1981); Dobbs v. Maine School Administrative District's No. 50, 419 A.2d 1024 (Me. 1980). OPMF argues that a better interpretation would be to read the first sentence of Section 713 consistently with the second which requires fully allocated costs, not marginal cost allocation. OPMF posits that there is no reason to believe that the Legislature intended the Commission to apply two different standards, particularly in light of the fact that the Commission had previously rejected marginal cost analysis in Cochrane (which was the motivation for the rate payer protection provisions of 35-A MRSA § 713). The Legislature would not have imposed a different allocation standard for rate payers without expressly saying so. See Caron v. Maine School Administrative District No. 27 594 A.2d 560 (Me. 1991). Thus, OPMF argues that CBITD's interpretation is contrary to rules of statutory interpretation and inconsistent with the foundational principles established in Cochrane.

OPMF argues that even if a fully allocated cost study would not affect the so-called "bottom line," it would allow CBITD rate payers to more accurately assess the costs associated with all of CBITD's services, including tour and charter. OPMF notes that CBITD strenuously argues that the islanders know best what works for them and that their decisions should not be usurped by the Commission. OPMF points out, however, that CBITD's argument assumes that the islanders are fully and accurately informed about the costs associated with CBITD's five vessel schedule and the costs associated with the purchase and operation of the *Bay Mist*.

OPMF claims that the record shows that CBITD has not been completely candid with its rate payers about the accounting methods it used to calculate the contribution that tour and charter makes to the bottom line. Specifically, in its March 1996 "Bayliner" newsletter, CBITD states that, "Each year we fully allocate all revenues and expenses to our various operations." Thus, according to OPMF, it is clear from the record that CBITD's rate payers have not been fully informed about all of the costs associated with providing tour and charter business and that a fully allocated cost accounting would assist them in becoming better informed.

3. OPA's Position

The OPA joins in OPMF's arguments that the first sentence of Section 713 should not be interpreted separately and

apart from the second sentence, which imposes a fully allocated cost standard. The OPA argues that the Legislature's intent was to require that there be fair compensation to utility rate payers when the utility's regulated assets are used to provide unregulated services and that this fair compensation should at least cover the fully allocated cost of the facility.

The OPA argues that the chief reason for instituting an accurate and reliable cost allocation procedure is to enable CBITD and the Commission to determine whether CBITD's regular customers are paying fares that are in line with the cost of its regularly scheduled service. Furthermore, when fully allocated accounting procedures are adopted, CBITD will be able to determine whether its unregulated tour and charter services are covering all of their costs.

4. Decision On Cost Accounting Method

We agree with CBITD that the first two protections found in Section 713 do not apply to CBITD because of its status as a ratepayer-owned, quasi-municipal utility. As noted earlier, when we promulgated Chapter 820 of our Rules, we did not consider whether CBITD should specifically be included or excluded from the coverage of the Rule. We did, however, exempt consumer-owned water utilities (COUs) from its application because we found that there would be no incentive for COUs to inappropriately shift costs from unregulated activities to the utility ratepayers. Docket No. 97-886, Requirements for Non-Core Utility Activities and Transactions Between Affiliates (Chapter 820), Order Provisionally Adopting Chapter 820 (July 8, 1998). We also noted that the activities of COUs are limited by the purposes set out in their legislative charters.

We find that the same rationale we used to exempt COUs from Chapter 820 applies here to exempt CBITD from the first two sentences of Section 713. Because CBITD is owned and managed by its rate payers, there is no incentive for CBITD to shift costs associated with tour and charter to its regular route rate payers. The procedural safeguards we implement today regarding

the proper sizing of CBITD's fleet further ensure that there will be no incentive to improperly shift tour and charter costs to rate payers. In addition, as was also noted above, the Legislature has specifically sanctioned CBITD's participation in the tour and charter market. Thus, we find that CBITD does not need to implement fully allocated cost accounting procedures.

C. CBITD Does Not Have An Undue Advantage In The Tour And Charter Market

The crux of OPMF's complaint in this case is that CBITD has an undue advantage in the competitive tour and charter market because of its regulated status and that this undue advantage violates Section 713. OPMF addresses a number of different advantages but focuses on the fact that CBITD can price its tour and charter services at marginal cost rather than at fully allocated cost. Both OPMF and OPA request that the Commission require CBITD to price its tour and charter services at or above its fully allocated costs for those services. CBITD responds by arguing that it currently prices at more than twice marginal cost in a manner that maximizes tour and charter revenue and that a fully allocated cost floor would result in a loss of revenue.

Resolution of this issue requires the Commission to choose between two conflicting statutes -- CBITD's enabling legislation and Section 713. Our decision today attempts to reconcile the conflicting nature of these statutes and reach a balanced resolution.

1. CBITD and OPMF compete in the same smaller charter market.

Before we can reach any conclusions regarding whether CBITD has an undue advantage in a competitive market, we must first establish whether CBITD and OPMF compete in the same market.

a. OPMF's Position

OPMF has consistently argued that it competes in the same market as CBITD. OPMF provides dinner cruises, lobster bakes, theme cruises, harbor tours, and private charters. CBITD provides tours and cruises to Bailey Island, tours on advertised regularly scheduled trips, music cruises, private charters and lobster bakes. OPMF witness Mr. Libby testified that 81% of OPMF's business is derived from services it provides in competition with CBITD. OPMF witness Mr. Ashton testified that CBITD does not serve a different market than OPMF because both CBITD and OPMF offer waterborne tours and charters service in and around Casco Bay.

In its Brief, OPMF points out that while CBITD claims that it does not compete in the same market, its witnesses have admitted that competition affects CBITD tour and charter prices. Further, OPMF claims that internal CBITD documents confirm its point, including a 1996 analysis by CBITD's Sales Director which attributed the loss of 1996 tour and charter revenue to CBITD's competition with OPMF. In addition, OPMF points to a document relating to the purchase of the *Bay Mist*, in which the Sales Director asked CBITD's Board of Directors, "How do we keep peace with the competition?"

b. CBITD's Position

Throughout this proceeding and throughout its briefs and testimony, CBITD has claimed that it does not compete in the same tour and charter market as OPMF. CBITD acknowledges that there is some overlap in the markets that it and OPMF serve but notes the following distinctions:

- (i) CBITD provides service with large, steel, double-decked vessels that have a minimum capacity of 300 passengers and average capacity of 340 passengers. The other tour and charter operators in Casco Bay operate 8 much smaller vessels, ranging from 36 to 149 passengers, with an average capacity of 76.5 passengers. Further, almost all such vessels are single-decked.
- (ii) More than 75% of CBITD's charters are to groups of 150 passengers or more which the other operators cannot transport.
- (iii) CBITD is not the largest tour and charter operator in Casco Bay. OPMF is the largest, with 43.2% of the tour and charter market compared to the Transit District's 36.8% share.
- (iv) CBITD's primary competitors are shoreside entertainment facilities, such as various restaurants (including the restaurant at Diamond Cove and DiMillo's floating restaurant), the Sea Dogs, LL Bean and Freeport, etc.
- (v) The other tour and charter operators focus on services not provided by CBITD, such as deep sea fishing, whale watches, and dinner cruises. CBITD points out that while the Bay Mist was a dinner cruise boat in its former life, CBITD has removed the galley equipment because it had no interest in providing dinner cruises.

c. Our Decision on Competition In the Tour and Charter Market

Despite CBITD's claims to the contrary, the evidence in this proceeding indicates that it competes directly with OPMF for charters of 150 passengers or less. Specifically,

approximately 20-25% (see ii above) of CBITD's tour and charter business competes directly with the smaller tour providers such as OPMF. OPMF's vessel *The Casablanca* has a capacity of 149 passengers and provides dinner, music, and other types of cruises and charters around the islands of Casco Bay. CBITD's vessels are much larger than the *Casablanca* but often serve groups of 150 or less. While CBITD does not conduct dinner cruises *per se*, it provides a functional equivalent with its charters that cruise Casco Bay and land on Peak's Island for a lobster bake. CBITD also conducts music cruises and general cruises around Casco Bay. An organization with 100 persons that wished to charter a cruise on Casco Bay would likely consider both CBITD and OPMF.

The record is equally clear, however, that CBITD and OPMF do not compete in the markets for: charters for groups over 150 passengers; whale/seal watching tours; and passenger travel to single islands (OPMF, if fact, is prohibited by 35-A M.R.S.A. § 5101 from providing this type of business). Based on CBITD witness Mr. Phipps' testimony that 99 out 127 charters in 1998 were for 150 or more passengers, it appears that between 78% and 80% of CBITD's current business includes 150 or more people.

The record is unclear regarding whether OPMF and CBITD compete in the regularly scheduled tour market. CBITD's tour business is fundamentally different from OPMF's in that, with the exception of the Bailey Island tour, CBITD's tours all require the boat to make specific scheduled stops at various islands (because the tour boat is in fact regular route Down Bay service). OPMF is not similarly limited and is free to tour the harbor and the various lighthouses along the shoreline and is not required to make any stops. Thus, while there may be some overlap (i.e., tourists who do not care exactly where they go or what they see as long as they are out on the water), it is more likely that OPMF and CBITD serve different tour markets. Thus, we find that OPMF and CBITD compete only in the same market for charters of 150 people or less (herein after small charters). While this finding does not affect our ultimate decision today, it may be relevant in the rulemaking we will commence to revise Chapter 520 of our Rules. (See Section VII below.)

2. CBITD does not have an undue advantage in the small charter market.

Having determined that OPMF and CBITD compete in the same small charter market, we must decide whether CBITD has an undue advantage in that market because of its regulated status. OPMF and OPA argue that CBITD does have an undue advantage because it can price its tour and charter services at marginal cost. CBITD argues that it prices at more than twice

marginal cost and that it does not have an undue advantage in the market.

a. OPMF's Position

OPMF claims that CBITD enjoys an undue advantage because of its many operational advantages and because it can price at marginal costs. OPMF claims that CBITD has made a concerted effort to use its status as a regulated ferry service provider to unfairly dominate and ultimately monopolize the competitive tour and charter market in Casco Bay.

OPMF first claims that CBITD's facilities provide it with operational advantages⁶ and that CBITD's year-round staff advances CBITD's tour and charter objectives. OPMF also claims that CBITD has financial advantages which act as subsidies that reduce CBITD's costs of operations and capital. Specifically, OPMF notes that CBITD's terminal facility is provided by the City of Portland at below market rent and that CBITD is exempt from income and sales tax requirements. Further, OPMF claims that all of CBITD's vessels are purchased with either federal government grants or tax-exempt bonds at rates unattainable in the commercial market. Finally, OPMF claims that CBITD receives substantial annual operating subsidies from the state, local and federal government.

OPMF next claims that CBITD has a clear advantage in the tour and charter market because it can price its charters at marginal cost rather than fully allocated cost. OPMF's Briefs detail its positions and we will not include all its arguments here. There are, however, several important points.

First, OPMF claims that CBITD currently prices its tour and charter services based upon a marginal cost allocation as adjusted by the IREA. OPMF witness Mr. Ashton claims that this provides CBITD with a competitive advantage because CBITD's monopoly over regulated ferry service allows it to charge higher rates to the captive regular route customers and lower rates to competitive tour and charter customers. Mr. Ashton analyzed the prices charged by other tour and charter operators in Casco Bay and concluded that CBITD charged

⁶OPMF cites as an example CBITD's modern, year-round terminal facility, a large parking garage, on-site administrative offices, indoor ticket and waiting area, outdoor sheltered waiting areas and public space, tour bus transfer and waiting areas, wide and stable passenger transfer facilities on the mainland and on regulated islands, on site berthing for its fleet and a fleet of five large (300+) passenger ferries with ample space for passengers and charter parties.

significantly less (17%) than its competitors for similar services. OPMF also points out that although CBITD has twice increased its summer rates for regular ridership since 1993 (in 1996, and again in 1997) to offset operating losses, it has not raised tour and charter rates since that time.

Second, OPMF claims that CBITD tries to make maximum use of its excess capacity for tour and charter by keeping its prices low. OPMF points out that under CBITD's view that any money it receives over marginal cost for tour and charter helps its bottom line, CBITD feels free to discount tour prices and "cut a deal" to get or keep charter business.

OPMF claims that it cannot raise its prices higher than the prices charged by CBITD, and thus it is put in the position of charging artificially low prices which do not cover its costs, while CBITD can charge the same prices and recover any losses from its regular route customers. OPMF argues that this "price driven competition" in the tour and charter business is causing it to lose money and that it will be driven out of business if the Commission does not intervene. Thus, OPMF claims that CBITD's failure to allocate all the costs of tour and charter service results in: (1) prices for tour and charter services being set artificially low, "which jeopardizes the economic viability of the competitive market for these services"; (2) rate payers subsidizing CBITD's tour and charter business; and (3) CBITD experiencing unfair competitive advantage in the tour and charter line of business.

OPMF also claims that CBITD's IREA analysis⁷ fails to accurately allocate all of the costs associated with CBITD's tour and charter services. OPMF witness Mr. Ashton claims that there are five adjustments that must be made to the IREA in order for it to reflect fully allocated costs for tour and charter service. First, CBITD's allocation of advertised tours is co-mingled and fails to properly account for the tour (unregulated) aspects of the service. Mr. Ashton claims that CBITD has not allocated either labor or vessel operating costs to tour and charter despite the fact that a portion of these costs was clearly incurred to provide services to the tour and cruise passengers who traveled on regular route vessels.

Mr. Ashton's second adjustment involves costs which have not been allocated at all to unregulated tours, including administrative labor costs, supervisory labor costs,

⁷CBITD claims that its Island Revenue and Expense Analysis is a fully allocated cost study based on the guiding principles of the U. S. Department of Transportation, Urban Mass Transportation Administration's Fully Allocated Cost Analysis - Guidelines for Public Transit Providers.

and terminal depreciation charges. Third, Mr. Ashton claims that CBITD failed to allocate some costs to either regulated or unregulated service leading to an overstatement of profits. Fourth, Mr. Ashton also notes that CBITD has not properly allocated some categories of shared costs between regulated and unregulated services. Costs such as operators, miscellaneous, and insurance fees and maintenance were all allocated to tour and charter on the basis of CBITD's "best estimates" and not based upon an analysis of the costs. Finally, Mr. Ashton notes that CBITD used incorrect allocation methods to allocate certain costs. Specifically, CBITD allocated depreciation on the basis of hours and miles of operation and ignores the reason the vessel was acquired.

OPMF posits that proper cost allocation procedures would result in a larger portion of CBITD's total costs being allocated to tour and charter. OPMF further argues that the Commission should require CBITD to set fares for tour and charter that recover its costs. OPMF supports OPA witness Rubin's recommendation (described below) that the Commission establish a price floor for tour and charter services based on the fully allocated cost of providing that service. OPMF argues that such a price floor would protect ratepayers from having to subsidize unregulated service and protect competitors from predatory pricing.

b. OPA's Position

The OPA argues that unless CBITD is required to use fully-allocated costs when it sets its prices for tour and charter services, CBITD will be in a better position competitively because many of its shared costs will be absorbed by its regulated operations. OPA witness Mr. Rubin testified that CBITD's competitors are adversely affected by CBITD's ability to assign much of the cost of unused capacity to its regulated operations because CBITD's regulated operations absorb a cost which is a direct cost of doing business for its competitors. The OPA argues that CBITD currently can set the prices for its unregulated services based on marginal costs and that its prices are artificially low. The OPA believes that by failing to allocate costs properly, CBITD is charging less than its cost (and less than competitors must charge) for tour and charter services -- which, in turn, jeopardizes the economic viability of the competitive market for those services. The OPA argues that this is exactly the type of advantage which is barred by Section 713.

Thus, OPA witness Mr. Rubin specifically recommends that the Commission establish a price floor for tour and charter services based on the fully allocated costs of providing that service. The OPA believes that this would protect

ratepayers from having to subsidize unregulated service and protect competitors from predatory pricing.

c. CBITD's Position

i. Non-pricing issues

CBITD's argues that Section 713 does not prohibit all competitive advantages -- only undue competitive advantages and thus, the fact that some competitive advantages exist should not compel the Commission to take any action. CBITD further argues that while the first two sentences of Section 713 apply to costs and payment of costs, the third sentence applies to non-cost items, such as preferential access to confidential customer information (name, address, payment history, and the like), mailing bills in a common envelope, and similar non-monetary practices. CBITD then points out that many of these advantages do not apply to it because its tour and charter customers (major employers and mainland groups) are different from its regular route customers (mostly the islanders).

CBITD also argues that many of the undue advantages alleged by OPMF are not the result of CBITD's regulated status. Specifically, advantages such as access to low interest borrowing, sales tax exempt status, no taxes on profits, etc., arise from CBITD's nonprofit status, not from its status as a regulated utility. Thus, CBITD claims that any non-monetary advantages identified by OPMF that arise from its regulated status are insignificant to the overall operations of both CBITD and the other tour and charter companies in Casco Bay, and that all such issues should be viewed as minor and not constituting "undue" competitive advantage.

ii. Cost allocation and pricing issues

While CBITD does not frame its Section 713 argument as including the pricing of tour and charter, it is clear that CBITD does not view its ability to price its tours and charters at marginal cost as an undue advantage because it says that it prices this service at more than two times marginal cost. CBITD argues that the Commission should not impose any price floors and that it should be allowed to continue its current pricing scheme because it maximizes profits to its rate payers.

CBITD's fundamental argument is that because it is owned by its rate payers, the rate payers directly benefit from each dollar of revenue from tour and charter service that exceeds the marginal cost of that service. CBITD claims that it is appropriate for a quasi-governmental organization to use its off-peak surplus capacity to provide services in competition with

the private sector so long as the services are priced to cover their marginal costs.

CBITD currently performs an IREA each year to determine whether each island is paying its fair share of the system's costs. CBITD claims that the IREA is a fully allocated cost study based on the guiding principals of the U. S. Department of Transportation, Urban Mass Transportation Administration's Fully Allocated Cost Analysis - Guidelines for Public Transit Providers. CBITD also states that based on the transportation guidelines, it allocates as many costs as possible directly to three primary cost centers: (1) vessel related expenses; (2) tour, cruises and charters; and (3) shore-side operations. The remaining costs, not directly allocated, are allocated between the various cost centers based on an analysis of each cost to determine the cost center with which it is associated.

CBITD witness Mr. Hagge states that the IREA was intended to be a fully allocated cost study only for the purposes of determining the relative costs for service to the various islands and whether relative ticket prices were fair. The study only allocates 70% of CBITD's total operating costs associated with the vessels' expenses. Mr. Hagge also claims, however, that the IREA can be easily modified to determine fully allocated costs for the remaining 30% of expenses by examining each individual cost category for shore-side expenses and then determining the appropriate standard to use for allocation.

CBITD witness Mr. Silkman supports Mr. Hagge's claim that the IREA is a reasonable attempt to perform a fully allocated cost study to evaluate relationships between the islands, not between the regulated and non-regulated businesses. He also agrees that the cost study could be easily modified to accommodate fully allocated costs to the tour and charter business. Specifically, Mr. Silkman proposes the following modifications and corrections:

- (1) disaggregate all revenues and costs included in the "miscellaneous" category under the tour and charter category of the study and allocate them to Peaks Island, Down Bay and Cruises;
- (2) allocate a portion of the actual terminal costs to the Cruises category; and,
- (3) allocate a portion of the on-boat labor costs to the mail boat and other non-Bailey Island cruises.

Mr. Silkman stresses, however, that a fully allocated cost study is not the appropriate study to determine the costs of providing various services, especially if the purpose is to determine whether certain services are being cross-subsidized to the detriment of competition in the market. Mr. Silkman asserts that truly fixed costs should not be considered when trying to determine if a service is being cross-subsidized because those costs will not vary with the provision of the service. In other words, because CBITD needs its vessels to provide regular route service, the fixed costs of those vessels (such as capital costs and depreciation) should not be included in calculating the price for using those vessels to provide tour and charter service.

CBITD next argues that it has every incentive to price its tour and charter services at a profit maximizing level and that it does set its prices at more than twice their marginal costs. CBITD claims that if it were to increase its tour and charter prices its total revenues would fall because demand would drop due to the higher prices. CBITD witnesses testified that it prices at the high end of the range of prices charged by other competitors and that the demand for tour and charter is elastic. Thus, in its Reply Brief, CBITD claims that if CBITD set tour and charter prices based on fully allocated costs, regular route rate payers would be \$100,000 worse off, despite the fact that rates for tour and charter would be higher than CBITD's current rates. It should be noted, however, that CBITD appears to have assumed that there will be a significant drop in demand for tour and charter.

d. Decision on Pricing of Tour and Charter Services

There have been no other complaints brought pursuant to Section 713 since its passage in 1997. While we did promulgate Chapter 820 earlier this year, as we have noted earlier, Chapter 820 is not applicable to CBITD. Thus, we are cognizant of the blank slate upon which we are writing and note that the decisions we reach here are based upon the unique facts and circumstances of this case. Today we find that neither the non-pricing advantages alleged by OPMF nor CBITD's ability to price its tour and charter services at marginal cost are undue advantages in violation of Section 713.

i. The alleged non-pricing advantages alleged by OPMF do not constitute undue advantage.

First, we agree with CBITD that many of the advantages alleged by OPMF are not due to CBITD's regulated status but instead due to the year-round nature of its business and its non-profit status. We also agree with CBITD witness Mr.

Silkman that it would not make sense to impose a royalty on the use of CBITD's goodwill because rate payers would be simply paying themselves. Thus, we find that the non-pricing advantages alleged by OPMF, such as year-round staffing and tax-exempt status, are not "undue advantages."

ii. CBITD's ability to price its small charters at marginal costs is not an undue advantage.

We agree with CBITD that Section 713 does not prohibit all competitive advantages a utility might have because of its status as a utility; it only prohibits undue advantages. We believe that the evidence in the record before us supports a finding that CBITD is currently pricing its tour and charter services at more than twice their marginal cost and thus not enjoying any undue competitive advantage. We find it unnecessary to institute a price floor as suggested by OPA and OPMF based on the theoretical possibility that CBITD could drop its prices to marginal cost.⁸

Exhibit A from CBITD's Reply Brief and CBITD's 1996-1997 Analysis Sales and Tour Department, (OPMF Ex. 9, Att. 11) (1997 Analysis) shows that the price CBITD currently charges for charters exceeds its average fully allocated cost. Exhibit A indicates that currently \$300,000 of costs are assigned to tour and charter. The Passenger Ferry Charter Analysis of the 1997 Analysis indicates that under the IREA study, charters account for approximately 18% of the total tour and charter costs. Using Line 3 of Column B of Exhibit A for the amount of costs CBITD would assign to tour and charter today (\$300,000) and multiplying by 18% we get \$54,000 of the total costs assigned to charters. Then, using the number of charters from 1997 (114), we are able to calculate an average cost per charter of \$474. If we ran the same calculation but used fully allocated costs as proposed by OPMF and OPA (Column C, Line 3 of Exhibit A)(\$500,000), the average cost is \$789. Both of these average costs are below the current charter rates which range from \$1100-\$1400 (excluding special school rates). Thus, CBITD's current rates are well above its costs no matter how they are calculated. We find it highly unlikely that CBITD would now lower its rates below its fully allocated or long-run marginal costs; CBITD's charter rates have been tariffed at above \$1000 since at least 1993.

We find that so long as CBITD's prices maximize its net revenues from the tour and charter business, rate payers will benefit because tour and charter revenues will provide some contribution, no matter how small, to CBITD's bottom

⁸See attached Dissent of Commissioner Diamond

line. CBITD should be free to price its tour and charter services at a profit-maximizing level so that rate payers receive the largest benefit possible.

While CBITD claims that its current prices are profit maximizing, they have not provided sufficient evidence to support such a finding. We agree with the OPA that CBITD should undertake a more formal analysis of its tour and charter business and carefully determine a profit-maximizing level for tour and charter prices. CBITD claims that the tour and charter market is elastic but has not presented any clear evidence of such elasticity. Further, even CBITD's own witness, Dr. Silkman, has criticized several aspects of CBITD's IREA analysis, which is the only cost analysis currently conducted by CBITD. We direct CBITD to adjust the IREA analysis as suggested by Mr. Silkman in his testimony and to undertake further analysis of what constitutes profit-maximizing pricing in the Casco Bay tour and charter market.

VII. DEFINITION OF INCIDENTAL

The final major issue raised in this Investigation is the interpretation of the phrase "incidental tour and charter" found in CBITD's enabling legislation. We must determine whether this phrase limits CBITD's ability to provide tour and charter, and if so, what those limits are.

A. CBITD's Position

CBITD contends that the Legislature's placement of the phrase "including incidental tour and charter service" in its charter reflects the Legislature's finding that providing tour and charter service was necessary to the Transit District and the islanders and was in the public interest. CBITD's charter provides that it may:

do things necessary to furnish waterborne transportation in this area, including incidental tour and charter service, for public purposes in the interest of public health, safety, comfort and convenience of the inhabitants of the islands comprising the district.

P&SL, 1981 Ch. 22, § 1. CBITD believes that the Legislature concluded that "incidental tour and charter service" was "necessary to furnish waterborne transportation," was itself a "public purpose," and was "in the interest of public health, safety, comfort and convenience" of the islanders.

CBITD acknowledges that while the phrase "including incidental tour and charter service" is a significant expansion of its powers, it is not unlimited. Rather, CBITD's tour and charter service must be "incidental" to CBITD's regular route operation. CBITD's lists five factors which indicate that this is so:

- (1) CBITD's operations give primary emphasis to its regular route service;
- (2) CBITD's vessels are all sized for regular route service;
- (3) CBITD schedules its vessels to provide the best regular route service possible;
- (4) CBITD provides tour and charter service only to the extent there is capacity not required for regular route service, either extra room on

existing trips or hours of the day when a vessel is not required for regular route service; and

- (5) In the event of conflicting demands for a vessel, the regular route need prevails. The Transit District stops selling tour tickets on runs likely to be near capacity and cancels charters if the vessel is needed for regular route service.

CBITD argues that it should be allowed to use all extra vessel capacity for tour and charter service because these services provide important revenue which supports the costs of regular route service. CBITD claims that tour and charter revenues have always been a significant revenue source and were relied upon when CBITD was created in 1981. CBITD points out that the percentage of its total revenue from tour and charter service has generally declined while the absolute level of those tour and charter revenues has generally increased. CBITD argues that the decrease in tour and charter revenue since 1995 confirms that it focuses primarily on its regular route service.

Finally, CBITD notes that in 1983 the Legislature was presented with a bill to delete the phrase "incidental tour and charter service" from the Section 1 of the Transit District's 1981 enabling legislation. During the legislative proceedings, the Maine Passenger Vessel Association claimed that the statutory change was necessary to prevent CBITD from competing in the tour and charter market and to reserve that tour and charter business for the other operators in Casco Bay. CBITD argues that the Legislature's rejection of the proposed amendment confirmed the Legislature's intention that CBITD continue to provide incidental tour and charter service in the way that service was then being provided - - for the direct benefit of the islanders in Casco Bay.

B. OPMF's Position

OPMF believes that we should interpret the phrase "incidental tour and charter" as a limitation upon CBITD's ability to use its fleet for tour and charter business. OPMF argues that because of concerns regarding Casco Bay Line's emphasis on tour and charter business, "incidental tour and charter" was included to ensure that, "CBITD did not repeat the sins of its predecessor CBL by emphasizing tour and charter services over its responsibility to provide regularly scheduled ferry service among and between the mainland and enumerated regulated islands." OPMF witness Mr. Thing, who operated CBL as the Bankruptcy Trustee, testified that the phrase was added to ensure that tour and charter did not become the primary scope of the operation.

OPMF argues that oversight of the relationship between CBITD's regulated ferry service and its unregulated tour and charter service requires the application of the principles the Commission has already announced and applied in its Cochrane decision and Chapter 820. Thus, OPMF argues that CBITD should not allowed to use the phrase "incidental tour and charter" to avoid the principles of fully allocated cost accounting and separation that apply to other utilities.

OPMF also points to a 1989 Commission report to the 114th Legislature on the operational limitations on CBITD's authority to conduct "incidental tour and charter" which stated that:

CBITD should not be allowed to add additional vessels to its fleet to increase its ability to provide tour and charter services.

The joint report went on to state that the interpretation of "incidental" should ensure that tour and charter revenues will remain "incidental" to CBITD's mission of providing regularly scheduled transportation services between the mainland and the Casco Bay islands.

Finally, OPMF believes that tying tour and charter to a percentage of CBITD'S overall revenue is "an invitation to CBITD to monopolize the tour and charter market." In support of its argument it points to past reports from the Commission to the Legislature which recommended that a percentage-based standard not be created and to CBITD's expert Mr. Silkman who testified that the percentage of overall revenue has nothing to do with CBITD's authorization to conduct "incidental" tour and charter service.

C. OPA's Position

The OPA recommends that the Commission define the word "incidental" so that it limits the extent to which the Transit District can subsidize its unregulated tour and charter service with the assets and revenues of its regularly scheduled ferry service. The OPA proposed the definition of "incidental tour and charter services" recommended by its witness Mr. Rubin: "the provision of tour and cruise service on regularly scheduled ferry runs as well as the use of only one additional vessel beyond those needed for regularly scheduled ferry service."

The OPA asserts that its definition will permit CBITD to sell tour, cruise, or charter tickets on regularly scheduled ferries. In addition, it would permit CBITD to have one vessel

as a standby or replacement in the event that another vessel requires repair or maintenance, or in the event that CBITD needs to provide extra service during peak periods. Under the OPA's definition, CBITD's use of one extra vessel for tour, cruise, or charter service would be "incidental" to its provision of regulated ferry service.

D. Decision on the Definition of Incidental

We believe that it is essential that CBITD's fleet be properly sized in order to ensure that CBITD's provision of tour and charter services remain incidental to its provision of regular ferry service. We believe that the safeguards we have adopted today regarding CBITD's future acquisition of additional capacity will adequately ensure that CBITD's fleet is properly sized for regular service. We also agree with OPMF and our own prior decisions that trying to limit CBITD to a certain percentage of revenues for tour and charter services would not adequately address the issue of excess capacity.

Accordingly, we find that CBITD should be allowed to provide tour and charter services with any excess capacity found within its properly sized fleet. Given our earlier finding regarding CBITD's need for a spare vessel, CBITD's excess capacity will include use of the spare boat when it is not needed for regular route service, excess space on regular route runs, and any idle or down time for vessels used in regular route service. The phrase "incidental tour and charter" will be defined as follows:

the provision of tour and cruise service on regularly scheduled ferry runs as well as the use of any unused capacity within CBITD's properly-sized fleet.

VII. CHAPTER 520'S RESTRICTIONS ON TOUR OPERATORS

Presently, under Chapter 520 of the Commission's rules, a charter vessel must remain dedicated to the group or person that it is serving during the duration of the charter. MPUC Chapter 520, Section 2(B)(ii). Charter operators are prohibited from dropping off passengers on an island and then returning later on another voyage to pick them up. If the charter passengers want to disembark onto the island, Chapter 520 requires that the charter boat must remain at the island and wait for those passengers to return, they may not return to Portland on CBITD vessels.

These limitations do not apply to CBITD. CBITD may sell tour tickets that allow its passengers to disembark from a boat

and return on another CBITD run. CBITD also allows a group to charter a boat one-way to the island and return to Portland on regularly scheduled ferry runs. Even CBITD's expert Mr. Silkman acknowledges that this is an unfair advantage and that all tour operators should be subject to the same rules.

Chapter 520 was intended to ensure that other tour operators did not infringe upon CBITD's regulated services -- the scheduled transportation of passengers to the islands in Casco Bay. As even CBITD admits, however, these Rules provide CBITD with a distinct advantage in the tour and charter market. We agree with CBITD, however, that this docket is not the appropriate docket to change our current rules. We had planned to institute a rulemaking on this subject last summer but delayed the start of that proceeding pending the outcome of this proceeding. We commit today to begin such a rulemaking so that the final rule will be completed prior to the 1999 tour and charter season.

Dated at Augusta, Maine this 11th day of December, 1998.

BY ORDER OF THE COMMISSION

Dennis Keschl
Administrative Director

COMMISSIONERS VOTING FOR:

Welch
Nugent
Diamond

CONCURRING IN PART AND
DISSENTING IN PART. SEE
ATTACHED DISSENT

NOTICE OF RIGHTS TO REVIEW OR APPEAL

5 M.R.S.A. § 9061 requires the Public Utilities Commission to give each party to an adjudicatory proceeding written notice of the party's rights to review or appeal of its decision made at the conclusion of the adjudicatory proceeding. The methods of review or appeal of PUC decisions at the conclusion of an adjudicatory proceedings are as follows:

1. Reconsideration of the Commission's Order may be requested under Section 1004 of the Commission's Rules of Practice and Procedure (65-407 C.M.R. 110) within 20 days of the date of the Order by filing a petition with the Commission stating the grounds upon which a reconsideration is sought.
2. Appeal of a final decision of the Commission may be taken to the Law Court by filing, within 30 days of the date of the Order, a Notice of Appeal with the Administrative Director of the Commission, pursuant to 35-A M.R.S.A. § 1320 (1)-(4) and the Maine Rules of Civil Procedure, Rule 73 et seq.
3. Additional court review of constitutional issues or issues involving the justness or reasonableness of rates may be had by the filing of an appeal with the Law Court, pursuant to 35-A M.R.S.A. § 1320 (5).

Note:

The attachment of this Notice to a document does not indicate the Commission's view that the particular document may be subject to review or appeal. Similarly, the failure of the Commission to attach a copy of this Notice to a document does not indicate the Commission's view that the document is not subject to review or appeal.